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IN THE

Supreme Court of the United States

OCTOBER TERM, 1939.

No. 30.

THE UNITED STATES OF AMERICA,
Petitioner,

v.

THE GLENN L. MARTIN COMPANY,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

BRIEF FOR THE RESPONDENT.

JOHN T. KOEHLER,
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Attorneys for Respondent.

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OPINIONS BELOW.

The opinion of the District Court (R. 10-14) is reported in 23 F. Supp. 262. The opinion of the Circuit Court of Appeals (R. 26-31) is reported in 100 F. (2d) 793.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered January 9, 1939 (R. 31). The petition for cer-

tiorari was filed April 8, 1939, and was granted May 1, 1939 (R. 32). The jurisdiction of this Court rests on Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925 (c. 229, 43 Stat. 938; 28 U. S. C. A. sec. 347).

QUESTIONS PRESENTED.

1. Under a Government supply contract providing for an increase of the stipulated purchase price to reimburse the contractor for any "* * * other taxes or charges * * * imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for * * *" by the contract, is the contractor entitled to reimbursement for taxes subsequently imposed under Titles VIII and IX of the Social Security Act and allocated to the cost of performing this particular contract?

2. Are unemployment insurance taxes "* * * paid by the contractor * * *" to a state within the meaning of the "* * * other taxes or charges * * *" described in Question 1, such taxes being paid to a state pursuant to a law enacted after the adoption of the Social Security Act and neither increasing nor decreasing the total amount of unemployment insurance taxes (state and federal) payable by the contractor after the Social Security Act became effective?

STATUTES INVOLVED.

The relevant portions of Titles VIII and IX of the Social Security Act, and of the Maryland Unemployment Compensation Law, are set out in the Appendix, *infra*, pp. 19-23.

STATEMENT.

Most of the facts (none of which are in dispute) have been set forth in the petitioner's brief (pp. 2-4). In addition, the facts as stipulated reveal that the contract was a standard form of Government contract (R. 4), and the petitioner, in its petition for a writ of certiorari, stated (p. 8) that "Almost all government contracts since 1933 have contained provisions either identical with that here involved, or so similar as to present substantially the same question."

SUMMARY OF ARGUMENT.

I. The social security taxes paid by the respondent constituted an additional cost of labor engaged in the performance of the contract. Since labor is an essential element of production and since the purpose of the contractual provision was to protect the respondent against loss arising from the imposition of new or additional federal taxes which would increase his cost of production, but which could not be anticipated, the payroll taxes so imposed and paid are clearly "* * * applicable directly upon production, manufacture, or sale of the supplies called for * * *" within the meaning of the contract. Since the language of a contract must be interpreted in the light of the circumstances existing at the time of its execution, it is erroneous to assume that the parties intended to give such language a technical construction wholly at variance with the purpose they sought to achieve.

II. The social security taxes paid by the respondent are recoverable in full since they were imposed by Congress and were paid by the respondent. The taxes imposed under Titles VIII and IX of the Social Security Act do not cease to be so imposed simply because Con-

gress gave taxpayers permission to pay a portion of such federal tax by means of a credit against similar taxes which might be payable under state unemployment compensation laws. In addition, the contract plainly did not require payment of any portion of the tax to the Federal Government as a condition precedent to recovery.

III. Since the contract was drafted in its entirety by the petitioner, the rule of construction which requires a contract to be interpreted most strongly against the party responsible for doubtful language should be applied here, and it is of no significance that the Federal Government happens to be the party against whom the rule is invoked.

ARGUMENT.

I.

THE SOCIAL SECURITY TAXES PAID BY THE RESPONDENT CONSTITUTED AN ADDITIONAL COST OF AN ESSENTIAL ELEMENT OF PRODUCTION OR MANUFACTURE AND WERE, THEREFORE, APPLICABLE DIRECTLY UPON PRODUCTION, MANUFACTURE OR SALE OF THE SUPPLIES CALLED FOR.

A. Article 17 (3) of the Contract Should Be Read in the Light of the Business and Accounting Principles Which Governed the Parties.

The contract between the petitioner and the respondent was signed on June 28, 1934, more than thirteen months before the Social Security Act was enacted (R. 4, 11). Article 17 (3) of the contract, after stating that the stipulated prices included "any Federal Tax heretofore imposed by the Congress which is applicable to the material called for" (R. 1-2, 10), provided further that:

> "If any sales tax, processing tax, adjustment charge and other taxes or charges are imposed or

changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for, then the prices herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change wil be charged to the Government and entered on vouchers as separate items."

The general purpose of this clause was, as the District Court stated (R. 12) "* * * to indemnify the contractor against increased costs of production due to increased taxes imposed by subsequent Acts of Congress * * *". The Circuit Court of Appeals stated (R. 29) that "* * * the provision was evidently inserted to protect the contractor against loss arising from the imposition of new or additional federal taxes, which would increase his cost of production but could not be anticipated with any degree of accuracy; and no tax could more clearly fall within the class of taxes which it was the purpose to provide against than an employment tax measured by the earnings paid to produce the articles which the contract called for." It follows that the language of the second sentence of Article 17 (3) was inserted in the contract partly to protect the contractor from being called upon to bear the burden of new or increased federal taxes which could not be anticipated (R. 29), and partly to prevent the contractor from submitting an excessive bid, the justification for such bid being that an allowance for a possible increase in present taxes or the enactment of new taxes would be a necessary protective measure.

Since there is no dispute concerning the purpose of Article 17 (3), this Court is asked to determine whether or not, with respect to social security taxes, the language used by the parties to effect that purpose falls short of the mark. In considering this question, it seems erroneous to assume, as the petitioner does, that the language of a business contract must be construed in the light of finely-drawn legal distinctions among various types of excises. To do so is to assume that the parties to the contract were aware of such distinctions and acted accordingly. It would seem to be more reasonable and more in accordance with the facts to assume that a business contract should be interpreted in accordance with principles of good business practice and sound accounting procedure, since both parties must be deemed to have signed the contract with such principles in mind. This is particularly true in the present case since the methods of accounting employed by the respondent conformed to a standard code of accounting approved by the petitioner (R. 7), were subjected to a daily examination during the period of performance (R. 7) and stand approved at the present time (Br. 9-10). It follows that the language of Article 17 (3) should be read in the light of the business and accounting principles which governed the parties thereto. *Miller v. Robertson*, 266 U. S. 243; *Canal Co. v. Hill*, 82 U. S. 94; *Gilmartin v. Princeton Bank & Trust Co.*, 80 F. (2d) 130 (C. C. A.-4). If the contract as so interpreted reveals that the respondent was to be protected against new taxes subsequently imposed by Congress, which, in accordance with sound business principles, increased its direct production costs, then such protection should not be denied.

B. As a Matter of Accounting, Social Security Taxes Are Applicable Directly Upon Production Because They Constitute an Additional Cost of Labor.

Under the method of accounting employed by the respondent, social security taxes paid by it on the direct labor engaged in the performance of the contract amounted to $5,616.06, while such taxes paid on overhead labor so engaged amounted to $2,131.26, making a total of $7,737.32, the amount for which suit was brought (R., 6, 28). It is conceded that this allocation was in accordance with correct accounting principles (Br. 10, R. 28). The Circuit Court of Appeals decided (R. 28) that the social security taxes paid on both direct and indirect labor engaged in the performance of the contract were recoverable. The petitioner does not assert, in its "Specification of Errors to be Urged" (Br. 5), or elsewhere, that the lower Court erred in so holding and does not claim that, within the meaning of Article 17 (3) of the contract, any distinction should be drawn between social security taxes paid on direct labor and like taxes paid on indirect labor. It follows that the sole question before this Court is whether or not the words "* * * other taxes or charges * * * made applicable directly upon production, manufacture, or sale of the supplies called for * * *" include payroll taxes on labor engaged in the performance of the contract.

The respondent's method of accounting required *all* taxes, except federal and state income taxes, to be included in overhead (R. 7). Consequently sales taxes, processing taxes and, following their subsequent enactment, social security taxes were all accorded the same accounting treatment. Article 17 (3) of the contract designates sales and processing taxes as examples of ex-

cise taxes "applicable directly upon production, manufacture, or sale" and the petitioner admits, of course, that such taxes would clearly be recoverable (Br. 9).[1] In determining the meaning of the words "applicable directly," it is, therefore, of no significance that the respondent was required to charge all excises, including social security taxes, to overhead and the petitioner does not so contend. To assert otherwise would be to deny the recovery of *any* excise tax imposed by Congress and would strike Article 17 (3) in its entirety from the contract. It follows that the "complicated accounting procedure" (Br. 9) of the respondent which "illustrates the indirect relation of the Social Security taxes to manufacture or production" (Br. 10) was equally applicable to taxes admitted to be "applicable directly upon production, manufacture, or sale".

The difficulties encountered by the petitioner in construing the words "applicable directly" arise, it is submitted, from a failure to interpret such words in accordance with accepted principles of business practice and accounting procedure. Cost accountants agree that the basic elements of the costs of production (manufacturing costs) are material, labor and other expenses, and that

[1] The petitioner does not specify what taxes other than sales and processing taxes might be recovered and relies upon the principle of *ejusdem generis* to limit the words "other taxes or charges" (Br. 9). However, the rule of *ejusdem generis* is merely a rule of construction to ascertain intention when such intention cannot be gathered from the context. *Helvering v. Stockholms Enskilda Bank*, 293 U. S. 84, 89. It is only an illustration of the broader maxim *noscitur a sociis* and, where applicable, does not require that the general terms following the specification of particular things or classes be rejected, but that such terms shall be deemed to include all things or classes which, though not enumerated, fall within such classification. *R. E. Durall Co. v. W., B. & A. Electric R. R. Co.*, 51 F. (2d) 566, 570 (C. C. A. 4); *Williston on Contracts* (1936 Ed.) sec. 619, citing *Swift & Co. v. Columbia Ry. etc. Co.*, 17 F. (2d) 46 (C. C. A. 4); and *Cleveland Transit Co. v. Consolidated Gas etc. Co.*, 55 F. (2d) 211 (C. C. A. 4). Any excise tax, therefore, applicable directly upon production manufacture or sale, falls within the words "other taxes or charges".

each of these elements is, in turn, divided into *direct* and *indirect* costs.[2] The distinction between direct and indirect costs of production is that "* * * the former are incurred directly for and are chargeable to specific cost units (material, labor and expense) while the latter are incurred for the productive process as a whole and must be spread over the cost units involved on some more or less arbitrary basis."[3] (Matter in parenthesis supplied.)

Viewed in the light of the foregoing principles, the meaning of the words "applicable directly upon production, manufacture, or sale" becomes clear. Processing taxes on materials, for instance, are *direct* expenses which increase or follow the direct cost of such materials and are, therefore, "appplicable directly" upon such cost. Capital stock taxes and stamp taxes, similar to light, heat, insurance and costs of a like nature, are examples of *indirect* expenses which do not increase or follow direct material or labor costs and are, therefore, applicable only indirectly upon production costs.[4] Income and excess profits taxes are neither directly nor indirectly applicable to production costs, since they are imposed on earnings and are not an item of cost (R. 7).

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[2] *Reitell—"Cost Accounting—Principles and Methods"*, pp. 24-28 (International Textbook Co.—1933); *Accountants Handbook*, p. 1282 (2nd Ed.) Ronald Press—1932.

[3] *Accountants Handbook op. cit.* p. 1282. A *direct* material cost or charge is the raw material from which the finished product is made; an *indirect* material cost or charge is material necessary to the processes of manufacture, but not forming a part of the finished product, i. e., operating supplies used in production. Similarly, *direct* expenses are "* * * expenditures which pertain to or follow either direct material or direct labor, so as in reality to be a part of either the one or the other * * *", while *indirect* expenses are expenditures which "* * * arise from the necessity of providing a place to work in, power to operate machines, and other requirements of a similar nature." *Reitell—op. cit.* p. 26.

[4] *Holmes—"Auditing—Principles and Procedure"*, p. 374 (Business Publications, Inc. 1939).

The distinction between processing taxes (direct expenses which increase direct material costs) and capital stock taxes (indirect expenses which do not increase direct material costs but are chargeable only to indirect expenses as manufacturing overhead) illustrates the proper meaning to be given to the words "applicable directly upon production, manufacture, or sale". Social security taxes are clearly *direct* expenses which increase labor costs.[5] The concensus of accounting opinion is that payroll taxes on labor are an additional cost of that labor (direct expense) and are not to be considered a cost of facilities and services for making the labor more effective (indirect expense).[6] It follows that a tax which is sufficiently direct in nature to be regarded by accountants as a part of an admittedly direct charge (labor) to production or manufacture is "applicable directly" upon such production or manufacture. Consequently, *both* processing taxes and social security taxes are *direct* expenses which are properly included in, and form a part of, material and labor costs. To admit that the former is "applicable directly upon production, manufacture, or sale" and, at the same time, to assert that the latter is not so applicable is to do violence to the principles of accounting which governed the parties to the contract.

It is well settled that courts of law will recognize and apply standard principles of accounting in order to determine the proper meaning to be attributed to words

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[5] *Sherwood-Culey—"Auditing Theory and Practice"*, pp. 372, 445 (South-Western Publishing Co. 1939); *Neuner—"Cost Accounting"*, p. 190, (Business Publications, Inc. 1938).

[6] *National Association of Cost Accountants Bulletin*, Vol. XVIII, No. 24, pp. 1376-77 (1937). In a subsequent report (N. A. C. A. Bulletin, Vol. XX, No. 3, pp. 187, 188, 193 (1938)), the Association stated that examination of the accounting treatment of payroll taxes by 639 manufacturing companies revealed that the great majority of such companies treated payroll taxes as a direct charge to labor.

which have acquired a definite business significance. *Eisner v. Macomber*, 252 U. S. 189, 209; *Bowers v. Kerbaugh-Empire Co.*, 271 U. S. 170; *Dayton Power & Light Co. v. Public Utilities Commission*, 292 U. S. 290; *Lindheimer v. Illinois Telephone Co.*, 292 U. S. 151, 168; *Lone Star Gas Co. v. Texas*, 304 U. S. 224. This would seem to be particularly true where, as in the present case, such principles of accounting were, in effect, incorporated in the contract (R. 7) and where the application of such principles was subject to the daily scrutiny and approval of the petitioner during the entire period of performance (R. 7).

C. As a Matter of Law, Social Security Taxes Are Applicable Directly Upon Production Because They Constitute an Additional Cost of Labor.

The petitioner refuses to include social security taxes within the scope of the contractual indemnity against future excise taxes on the ground that the nature of this particular type of excise (a tax on the relation of employment) prevents it from being either *directly or indirectly* applicable upon production, manufacture or sale (Br. 8). This argument was characterized by the District Court as "* * * a construction of the wording which seems very narrow and literal" (R. 12) and was unqualifiedly rejected by the Circuit Court of Appeals (R. 28). The petitioner admits that, if this argument is sound, social security taxes "* * * are not 'applicable' upon production, manufacture or sale at all * * *" (Br. 8).

The last sentence of the preceding paragraph illustrates that a failure to give the words "applicable directly" the meaning accorded them by the parties may result in an interpretation which clearly lacks plausibility.

Just as the words of a statute must be read in their plain popular meaning (*Woolford Realty Co. v. Rose*, 286 U. S. 319), so the words of a contract must be given the meaning the parties obviously intended. *United States Fidelity & Guaranty Co. v. French Mutual General Society*, 212 Fed. 620 (C. C. A. 4). To say that a tax which directly increases the cost of production or manufacture is not applicable to (i. e., does not affect) that cost is to do violence to the normal meaning attributable by business men to the words "applicable directly".

This Court has already decided that a tax upon the relation of employment is none the less a tax applicable upon production. In *Carmichael v. Southern Coal Co.*, 301 U. S. 495, 524-525, this Court, speaking through Mr. Justice STONE, stated:

> "The Alabama legislature may have proceeded upon the view, for which there is abundant authority, that the causes of unemployment are too complex to admit of a meticulous appraisal of employer responsibility. It may have concluded that unemployment is an inseparable incident of modern industry, with its most serious manifestations in industrial production; that employees will be best protected, and that *the cost of the remedy, at least until more accurate and complete data are available, may best be distributed, by imposing the tax evenly upon all industrial production, and in such form that it will be added to labor costs* which are ultimately absorbed by the public in the prices which it pays for consumable goods." (Italics supplied.)

It follows that a tax may still be "applicable directly upon production, manufacture, or sale" within the meaning of the contract in this case, even though the nature of such tax has been stated to be "upon the relation of employment."

The petitioner, in searching for a construction of the words "applicable directly" apart from the accepted meaning ascribed to them in this brief, enters the fields of federal taxation and interstate commerce (Br. 11-13). Although the present case is not a suit for the refund of taxes, but is simply an action for breach of a contract (R. 1), it is perhaps pertinent to observe that the case of *Liggett & Myers Co. v. United States*, 299 U. S. 383 (Br. 12) is authority for the proposition that a tax on tobacco prior to its sale to a state imposes only an indirect burden on the state. This burden was held to be indirect because the tax was imposed, not on the state, but on the manufacturer who sold it the tobacco. Had the respondent sought to recover payroll taxes paid by a manufacturer on goods sold to the respondent, the cited case might have some bearing here. It can, however, have no appplication where the tax is imposed directly upon a manufacturer who later sues to recover it.

The interstate commerce cases cited by the petitioner (Br. 12-13) hold that a tax on a privilege or franchise "equal to" or "measured by" gross receipts amounts to a direct tax on such receipts, regardless of the wording of the particular statute. Consequently, if such gross receipts are derived from interstate commerce, the tax is invalid as a direct burden upon such commerce. It would seem, therefore, that the cited cases are authority for the proposition that this Court will consider the nature and effect of a tax regardless of the particular language in which it may have been couched. As was said in *Crew Levick Co. v. Pennsylvania*, 245 U. S. 292, 294:

> "As in other cases of this character, we accept the decision of the state court of last resort, respecting the proper construction of the statute, but are in

> duty bound to determine the questions raised under the Federal Constitution *upon our own judgment of the actual operation and effect of the tax, irrespective of the form it bears or how it is characterized by the state courts.*" (Italics supplied.)

It is respectfully submitted that this language is equally applicable to the facts of the instant case and that a tax "upon the relation of employment" does not cease to be a tax which directly affects, or is "applicable directly" upon, production or manufacture by increasing the cost of an essential element thereof. It follows that the social security taxes sought to be recovered fall squarely within the language of Article 17 (3), that the words "applicable directly upon production" include all taxes which directly increase production costs and exclude all others, and, finally, that such words should be read in the light of the meaning attributable to them by the parties and not in the light of technical differences attributable to various types of excises.

II.

THE SOCIAL SECURITY TAXES PAID BY THE RESPONDENT ARE RECOVERABLE IN FULL SINCE SUCH TAXES WERE IMPOSED BY CONGRESS AND WERE PAID BY THE RESPONDENT.

The petitioner urges (Br. 14-18) that the parties did not intend the respondent to be reimbursed for any taxes imposed by Congress unless such taxes were actually paid to the Federal Government. This argument loses sight of the fact that the contract provided for the recovery of "* * * other taxes or charges * * * imposed or changed by the Congress subsequent to the date of this contract and * * * paid by the Contractor on the articles or supplies herein contracted for * * *". It will be noticed that payment "to the Federal Govern-

ment" is not a prerequisite to recovery. *Batavia Mills, Inc., v. United States*, 85 Ct. Cls. 447, is directly in point.

The argument pressed here by the petitioner was so well answered by the Circuit Court of Appeals that the respondent feels that any attempt to parallel the cogent reasoning of the lower Court would be ineffectual. Accordingly, the second portion of the opinion of the Circuit Court of Appeals is here reproduced in full. Speaking for the Court, Judge PARKER stated (R. 30-31):

> "Coming to the second question, i. e., whether the portion of the tax paid to the State of Maryland and credited against the tax due under the Act to the federal government falls within the meaning of the clause of the contract under consideration, it is to be noted that this portion, as well as the remainder, falls squarely within the language used. The entire amount of the tax was 'imposed' by Congress and was 'paid by the contractor.' That a part of it was paid with the consent of Congress to the State of Maryland and credited against the amount which would otherwise have been due under the Act, would seem to be immaterial. A very similar question was before the Court of Claims in *Batavia Mills, Inc., v. United States* (decided June 1, 1937, but unreported). There, a processing tax on cotton yarn had been paid by the manufacturer of cotton cloth to the selier of the yarn pursuant to the terms of a contract under which the yarn was purchased. The manufacturer of the cloth had sold it to the government under a contract providing that the price should be increased by the amount of any new taxes made applicable by Congress to the supplies to be furnished after the date of the bid. In holding that the amount of the tax so paid might be recovered by the manufacturer of the cloth, who had not paid it to the government but to the processor of the yarn, the court said:

"'This is not a suit for the refund of taxes paid but an action based upon the provisions of a contract. The provisions of the law with reference to refunds of taxes collected under the Agricultural Adjustment Act have theretofore no application. All of the matter necessary to establish plaintiff's claim under the contract are shown. After the contract was entered into a new and additional tax was imposed on the manufacturer from whom the contract supplies were purchased by plaintiff. The tax was passed on by the manufacturer and under the terms of plaintiff's contract with the manufacturer it was obliged to pay it. *Defendant expressly agreed that the amount of the tax should be added to the purchase price.* The right of plaintiff to recover the amount so paid is clear and judgment will be rendered accordingly.'

"The Federal Social Security taxes were imposed by Congress as part of a comprehensive plan in which the states were expected to participate. That the states might be induced to do this, it was provided in the Act that the taxpayer might credit against the tax imposed by it any contributions paid by him into a state unemployment fund, to an amount not exceeding 90% of the amount of the tax under the federal Act. *This, of course, was no more than permission to the taxpayer to pay to the state 90% of the tax imposed by the Act and to credit same as a deduction on the federal tax;* and where the plaintiff availed itself of this privilege, paying a portion of the tax imposed to the state and claiming credit therefor under the Act, we think that it comes within the protection of the spirit as well as the language of the clause in the contract here-under consideration. *Even though the taxpayer was under legal obligation to pay the state tax to the state, the fact remains that that tax was imposed in connection with the general system*

brought into being by the federal Act and payment thereof was recognized as satisfying 90% of the obligation imposed by the federal tax. See Sections 903 and 904; *Steward Mach. Co. v. Davis*, 301 U. S. 548. If the state had not imposed a tax and established an unemployment fund complying with the requirements of the federal Act, the entire amount of the federal tax, without credit, would have been collected by the federal government and plaintiff would unquestionably have been entitled to recover same under the contract provision. We think it is in no worse plight because the state has seen fit to comply with the provisions of the federal Act and thus receive 90% of the tax that it imposes. *The clause of the contract was intended to protect plaintiff against new taxes to be imposed by the federal government. It should not be denied this protection because that government permits a portion of the taxes imposed to be paid to the states under a general scheme for state and federal cooperation.*" (Italics supplied).

That this Court is of the opinion that social security taxes paid under State unemployment compensation laws are paid to discharge a tax imposed by the Federal Government is evident from *Carmichael v. Southern Coal Co.*, 301 U. S. 495. In that case this Court declared (p. 507):

> "By §902 of the Social Security Act, contributors to the state fund are entitled to credit their contributions *in satisfaction of the tax imposed on employers by the Social Security Act*, to the extent of 90% of the tax. See *Chas. C. Steward Machine Co. v. Davis*, decided this day, post, p. 548" (Italics supplied).

III.

IF ANY DOUBTS EXIST CONCERNING THE MEANING OF ARTICLE 17 (3) THEY SHOULD BE RESOLVED AGAINST THE PETITIONER.

The contract here involved was a standard form of government supply contract and was admittedly drafted by the petitioner. The rule of construction which requires a contract, in case of doubt concerning the meaning of its language, to be construed most strongly against the party drafting it applies to the Federal Government as fully as if the Government were an individual. As this Court stated in *Reading Steel Casting Co. v. United States*, 268 U. S. 186, 188, a case in which the United States was a contracting party:

> "The contract is to be construed and the rights of the parties are to be determined by the application of the same principles as if the contract were between individuals."

To the same effect see *Garrison v. United States*, 7 Wall. 688, 690; *United States v. Smith*, 4 Otto 214, 217; *Marietta Mfg. Co. v. United States*, 73 Ct. Cls. 528, 546.

CONCLUSION.

The decision of the Court below is correct and should be affirmed.

Respectfully submitted,

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APPENDIX.

Social Security Act, c. 531, 49 Stat. 620:

TITLE VIII—TAXES WITH RESPECT TO EMPLOYMENT.

* * * * * * *

EXCISE TAX ON EMPLOYERS.

SEC. 804. In addition to other taxes, every employer shall pay an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 811) paid by him after December 31, 1936, with respect to employment (as defined in section 811) after such date:

(1) With respect to employment during the calendar years 1937, 1938, and 1939, the rate shall be 1 per centum.

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(U. S. C. Supp. IV, Title 42, Sec. 1004).

COLLECTION AND PAYMENT OF TAXES.

SEC. 807 (a). The taxes imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collection. * * *

(U. S. C. Supp. IV, Title 42, Sec. 1007).

DEFINITIONS.

SEC. 811. When used in this title—

(a) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash; except that such term shall not include that part of the remuneration which, after remuneration equal to $3,000 has been

paid to an individual by an employer with respect to employment during any calendar year, is paid to such individual by such employer with respect to employment during such calendar year.

(b) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

(Exceptions not pertinent).

(U. S. C. Supp. IV, Title 42, Sec. 1011).

TITLE IX—TAX ON EMPLOYERS OF EIGHT OR MORE.

Imposition of Tax.

SECTION 901. On and after January 1, 1936, every employer (as defined in section 907) shall pay for each calendar year an excise tax, with respect to having individuals in his employ, equal to the following percentages of the total wages (as defined in section 907) payable by him (regardless of the time of payment) with respect to employment (as defined in section 907) during such calendar year:

(1) With respect to employment during the calendar year 1936 the rate shall be 1 per centum;

(2) With respect to employment during the calendar year 1937 the rate shall be 2 per centum;

* * * * * *

(U. S. C. Supp. IV, Title 42, Sec. 1101).

Credit Against Tax.

SEC. 902. The taxpayer may credit against the tax imposed by section 901 the amount of contributions, with respect to employment during the taxable year, paid by him (before the date of filing his return for the taxable year) into an unemployment fund under a State law. The total credit allowed to a taxpayer under this

section for all contributions paid into unemployment funds with respect to employment during such taxable year shall not exceed 90 per centum of the tax against which it is credited, and credit shall be allowed only for contributions made under the laws of States certified for the taxable year as provided in section 903.

(U. S. C. Supp. IV, Title 42, Sec. 1102).

CERTIFICATION OF STATE LAWS.

SEC. 903 (a). The Social Security Board shall approve any State law submitted to it, within thirty days of such submission, which it finds provides that—

(1) All compensation is to be paid through public employment offices in the State or such other agencies as the Board may approve;

(2) No compensation shall be payable with respect to any day of unemployment occurring within two years after the first day of the first period with respect to which contributions are required;

(3) All money received in the unemployment fund shall immediately upon such receipt be paid over to the Secretary of the Treasury to the credit of the Unemployment Trust Fund established by section 904;

(4) All money withdrawn from the Unemployment Trust Fund by the State agency shall be used solely in the payment of compensation, exclusive of expenses of administration;

(5) Compensation shall not be denied in such State to any otherwise eligible individual for refusing to accept new work under any of the following conditions: (A) If the position offered is vacant due directly to a strike, lockout, or other labor dispute; (B) if the wages, hours, or other conditions of the work offered are substantially less favorable to the individual than those prevailing for similar work in the locality; (C) if as a condition of being employed the individual would be

required to join a company union or to resign from or refrain from joining any bona fide labor organization;

(6) All the rights, privileges, or immunities conferred by such law or by acts done pursuant thereto shall exist subject to the power of the legislature to amend or repeal such law at any time.

The Board shall, upon approving such law, notify the Governor of the State of its approval.

(U. S. C. Supp. IV, Title 42, Sec. 1103).

ADMINISTRATION, REFUNDS, AND PENALTIES.

SEC. 905 (a). The Tax imposed by this title shall be collected by the Bureau of Internal Revenue under the direction of the Secretary of the Treasury and shall be paid into the Treasury of the United States as internal-revenue collections. * * * (U. S. C. Supp. IV, Title 42, Sec. 1105).

DEFINITIONS.

SEC. 907. When used in this title—

(a) The term "employer" does not include any person unless on each of some twenty days during the taxable year, each day being in a different calendar week, the total number of individuals who were in his employ for some portion of the day (whether or not the same moment of time) was eight or more.

(b) The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash.

(c) The term "employment" means any service, of whatever nature, performed within the United States by an employee for his employer, except—

(Exceptions not pertinent).

(U. S. C. Supp. IV, Title 42, Sec. 1107).

Maryland Unemployment Compensation Law, Laws of Maryland, extraordinary Session, December, 1936, c. 1:

CONTRIBUTIONS.

7. (a) Payment.—

(1) On and after January 1, 1936, contributions shall accrue and become payable by each employer for each calendar year in which he is subject to this Act, with respect to wages payable for employment (as defined in section 19 (g) ocurring during such calendar year. Such contributions shall become due and be paid by each employer to the Board for the fund in accordance with such regulation as the Board may prescribe, and shall not be deducted, in whole or in part, from the wages of individuals in his employ.

(2) In the payment of any contributions, a fractional part of a cent shall be disregarded unless it amounts to one-half cent or more, in which case it shall be increased to 1 cent.

(b) Rate of Contribution.—

Each employer shall pay contributions equal to the following percentages of wages payable by him with respect to employment:

(1) Nine-tenths of 1 per centum with respect to employment during the calendar year 1936;

(2) One and eight-tenths per centum with respect to employment during the calendar year 1937;

(3) Two and seven-tenths per centum with respect to employment during the calendar years 1938 and thereafter.

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SUPREME COURT OF THE UNITED STATES.

No. 30.—October Term, 1939.

The United States of America, Petitioner, *vs.* The Glenn L. Martin Company.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

[November 6, 1939.]

Mr. Justice Black delivered the opinion of the Court.

We must determine whether a contract to purchase certain aircraft and aircraft material from respondent required the United States to increase the stipulated price by the amount of Social Security taxes paid by respondent.

June 28, 1934, the War Department and respondent, a Maryland manufacturer, made the contract, providing—

"It is expressly understood and agreed to by and between the parties hereto that the prices herein stipulated include any Federal Tax heretofore imposed by the Congress which is applicable to the material called for under the terms of this contract. If any sales tax, processing tax, adjustment charge, or other taxes or charges are imposed or changed by the Congress subsequent to the date of this contract and made applicable directly upon production, manufacture, or sale of the supplies called for herein and are paid by the Contractor on the articles or supplies herein contracted for then the price herein stipulated will be increased or decreased accordingly and any amount due the Contractor as result of such change will be charged to the Government and entered on vouchers as separate items."

With respect to payrolls of employees alleged to have been engaged in fulfilling this contract during 1936 and 1937, respondent paid $794.03 in Federal Social Security taxes and $6,943.29 under the State of Maryland's Unemployment Compensation Law. Both the Federal tax and Maryland's tax were levied "subsequent to the date of this contract." Respondent claims that both the Maryland Unemployment Compensation taxes[1] and the Federal Social Se-

[1] Laws of Maryland, extraordinary session, Dec. 1936, c. 1.

curity taxes[2] were "imposed . . . by . . . . Congress" and were of the type for which the contract provided extra compensation.

Rejecting respondent's construction of the contract, the District Court held that no part of the taxes paid by respondent served to increase the liability of the Government on its contract.[3] The Circuit Court of Appeals reversed[4] and we granted certiorari.[5]

Obviously, the seller fixed its stipulated prices so as to provide a margin of profit over Federal taxes for which it might at the time of the contract be responsible on the particular "material" sold. This clearly appears from the governing provision's opening declaration that "the prices herein stipulated include any Federal tax heretofore imposed by Congress which is applicable to the material called for under the terms of this contract." But, without more, future increases in Federal taxes "applicable to the material" might have substantially affected the margin of profit which the contract was calculated to insure. Against the contingency of increase in Federal taxes applicable to the "material" purchased, the Government undertook to compensate the seller for payment of future Federal taxes "on the articles or supplies contracted for" should Congress levy any sales tax, processing tax or other tax "applicable directly upon production, manufacture or sale of the articles . . . contracted for . . . . ."

But the Social Security Act[6] imposes upon every employer "an excise tax with respect to having individuals in his employ." And employment in that Act "means any service, of whatever nature, performed within the United States by an employee for an employer . . . " with exceptions not material here. This excise has been represented as one levied "upon the relation of employment"[7]

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[2] 49 Stat. 620, 637.

[3] 23 F. Supp. 262.

307 US 618

[4] 100 Fed. (2d) 793.

[5] U. S. . The government's petition for certiorari set out that "Almost all government contracts since 1933 have contained provisions either identical with that here involved, or so similar as to present substantially the same question. . . . The War Department alone . . . states that approximately 4,000 potential claims may arise under contracts with language identical with that in . . . the contract in this case." The Comptroller General of the United States has interpreted a contract substantially identical with the one under consideration as denying reimbursement for Social Security taxes. 16 Comp. Gen. 790 (1937). Certiorari was granted in order to obtain a final determination of the question.

[6] Social Security Act, c. 531, 49 Stat. 620, Sec. 804, 210(b).

[7] Steward Mach. Co. v. Davis, 301 U. S. 548, 578.

and upon "the right to employ"[8] and as a payroll tax.[9] It is not—as taxes upon the privilege of selling, manufacturing or processing characteristically are—measured by the value of the privilege taxed, or by either quantity or price of what is manufactured, processed or sold. A tax on the processing or sale of an article, while an excise, commonly would be denoted a tax "on" the article processed or sold. The contract itself speaks of such taxes which may, in the future, be "paid by the contractor *on* the articles or supplies contracted for." (Ital. supp.) Thus, this contract was concerned with Federal taxes "on" the goods to be provided under it, whatever the occasion for the taxes. And a tax "on" the relationship of employer-employee—characterized as a tax on payrolls—is not of the type treated by the contract as a tax "on" the goods or articles sold.

The contract refers only to Federal taxes, existing or future, on "material", "articles" or "supplies." And additional compensation is provided to offset only Federal taxes of the type of sales taxes and processing taxes, "applicable directly upon production, manufacture, or sale" and actually paid on supplies delivered to the Government. Since a tax on payrolls, or on the relationship of employment, is not—but in fact is distinct from—the type of tax "on" articles represented by sales taxes and processing taxes, respondent is not entitled to the additional compensation which it seeks.

In view of our determination that the Federal Social Security tax was not contemplated by the contract, we need not discuss respondent's contention that the tax paid under the Maryland Unemployment Compensation Act was a tax "imposed . . . by . . . Congress."

The judgment of the Circuit Court of Appeals is reversed and that of the District Court is affirmed.

Mr. Justice BUTLER took no part in the consideration and decision of this case.

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[8] See, Carmichael v. So. Coal Co., 301 U. S. 495, 508.

[9] *Id.*, 506, 511.